

any other non-competitive transactions, including block trades, should have rules particularly authorizing such transactions and establishing appropriate recordkeeping requirements. Block trading rules should ensure that the block trading does not operate in a manner that compromises the integrity of the prices or price discovery on the relevant market.

Registration Criterion 4 of section 5a(c) of the Act: *FINANCIAL INTEGRITY OF TRANSACTIONS—The board of trade shall establish and enforce rules or terms and conditions providing for the financial integrity of transactions entered on or through the facilities of the board of trade, and rules or terms and conditions to ensure the financial integrity of any futures commission merchants and introducing brokers and the protection of customer funds.*

(a) A board of trade operating as a registered derivatives transaction execution facility should provide for the financial integrity of transactions by setting appropriate minimum financial standards for members and non-intermediated market participants, appropriate margin forms, and appropriate default rules and procedures. If cleared, agreements, contracts and transactions in excluded or exempt commodities that are traded on a DTF may be cleared through clearing organizations other than DCOs registered with the Commission. The Commission believes ensuring and enforcing the financial integrity of transactions and intermediaries, and the protection of customer funds should include monitoring compliance with the facility's minimum financial standards. In order to monitor for minimum financial requirements, a facility should routinely receive and promptly review financial and related information.

(b) A registered derivatives transaction execution facility that allows customers that qualify as "eligible traders" under the definition found in section 5a(b)(3) of the Act only by trading through a registered futures commission merchant pursuant to section 5a(b)(3)(B), should have rules concerning the protection of customer funds that address appropriate minimum financial standards for intermediaries, the segregation of customer and proprietary funds, the custody of customer funds, the investment standards for customer funds, related recordkeeping procedures and related intermediary default procedures.

[66 FR 42271, Aug. 10, 2001, as amended at 71 FR 1964, Jan. 12, 2006]

#### APPENDIX B TO PART 37—GUIDANCE ON COMPLIANCE WITH CORE PRINCIPLES

1. This appendix provides guidance on complying with the core principles in order to maintain registration under Section 5a(d) of the Act and this part. This guidance is illus-

trative only and is not intended to be used as a mandatory checklist.

2. If a registered derivatives transaction execution facility chooses to certify that it has the capacity to, and upon initiation will, operate in compliance with the core principles under section 5a(d) of the Act and §37.6, it should consider the issues set forth in this appendix prior to certification.

3. Alternatively, if an applicant for registration or for reinstatement of registration under §37.6(b)(2) chooses to provide the Commission with a demonstration of its compliance with core principles, addressing the issues set forth in this appendix would help the Commission in its consideration of such compliance. To the extent that compliance with, or satisfaction of, the core principles is not self-explanatory from the face of the derivatives transaction execution facility's rules, (as defined in §40.1 of this chapter) a submission under §37.6(b)(2) should include an explanation or other form of documentation demonstrating that the derivatives transaction execution facility complies with the core principles.

Core Principle 1 of section 5a(d) of the Act: *IN GENERAL—To maintain the registration of a board of trade as a derivatives transaction execution facility, a board of trade shall comply with the core principles specified in this appendix.*

The board of trade shall have reasonable discretion in establishing the manner in which the board of trade complies with the core principles. A board of trade newly registered to operate as a derivatives transaction execution facility must certify or satisfactorily demonstrate its capacity to operate in compliance with the core principles under section 5a(d) of the Act prior to the commencement of its operations. The Commission also may require that a board of trade operating as a registered derivatives transaction execution facility demonstrate to the Commission that it is operating in compliance with one or more core principles.

Core Principle 2 of section 5a(d) of the Act: *COMPLIANCE WITH RULES—The board of trade shall monitor and enforce the rules of the facility, including any terms and conditions of any contracts traded on or through the facility and any limitations on access to the facility.*

(a) A board of trade operating as a registered derivatives transaction execution facility should have arrangements, resources and authority to detect and deter abuses by effectively and affirmatively enforcing its rules (which, in the case of a facility that restricts traders to eligible commercial entities, may be the effective monitoring of limitations on access to the facility), including the authority and ability to collect or capture information and documents on both a routine and non-routine basis and to investigate effectively possible rule violations.

(b) This should include the authority and ability to discipline, limit or suspend, and/or terminate activities or access of a member, including members with trading privileges but having no, or only nominal equity, in the facility and non-member market participants or, in the case of a derivatives transaction execution facility restricting its traders to eligible commercial entities, the authority and ability to terminate activities or access of such a member. In either case, any termination should be carried out pursuant to clear and fair standards that are available and transparent to the member or market participant.

Core Principle 3 of section 5a(d) of the Act: *MONITORING OF TRADING*—The board of trade shall monitor trading in the contracts of the facility to ensure orderly trading in the contract and to maintain an orderly market while providing any necessary trading information to the Commission to allow the Commission to discharge the responsibilities of the Commission under the Act.

(a) Arrangements and resources to detect and deter abuses through effective trade monitoring programs should facilitate, on both a routine and nonroutine basis, direct supervision of the market. Appropriate objective testing and review of any automated systems should occur initially and periodically to ensure proper system functioning, adequate capacity and security. The analysis of data collected should be suitable for the type of information collected and should occur in a timely fashion. A board of trade operating as a registered derivatives transaction execution facility should have the authority to collect the information and documents necessary to reconstruct trading for appropriate market analysis as it carries out its programs to ensure orderly trading and to maintain an orderly market. The facility also should have the authority to intervene as necessary to maintain an orderly market.

(b) Alternatively, if a board of trade operating as a registered derivatives transaction execution facility restricts contracts traded to those under §§37.3(a)(1) and 37.3(b), it may choose to satisfy this core principle by providing information to the Commission as requested by the Commission to satisfy its obligations under the Act. The facility should have the authority to collect or capture and retrieve all necessary information.

Core Principle 4 of section 5a(d) of the Act: *DISCLOSURE OF GENERAL INFORMATION*—The board of trade shall disclose publicly and to the Commission information concerning—(A) contract terms and conditions; (B) trading conventions, mechanisms, and practices; (C) financial integrity protections; and (D) other information relevant to participation in trading on the facility.

The Commission considers that the public disclosure of information required under the core principle refers to disclosure to market

participants, where the facility's user agreement requires all market participants to keep such information confidential. A board of trade operating as a registered derivatives transaction execution facility should have arrangements and resources for the disclosure and explanation of contract terms and conditions, trading conventions, trading mechanisms, trading practices, system functioning, system capacity, and financial integrity protections, including whether eligible contract participants will have the right to opt out of segregation of customer funds. Such information may be made publicly available through the derivatives transaction execution facility's website. The facility should also, as appropriate to the market, make information regarding prices, bids and offers, or other information as determined by the Commission, readily available to market participants on a fair, equitable and timely basis. Furthermore, the facility should make available information concerning steps taken by the facility in response to an emergency.

Core Principle 5 of section 5a(d) of the Act: *DAILY PUBLICATION OF TRADING INFORMATION*—The board of trade shall make public daily information on settlement prices, volume, open interest, and opening and closing ranges for contracts traded on the facility if the Commission determines that the contracts perform a significant price discovery function for transactions in the cash market for the commodity underlying the contracts.

A board of trade operating as a registered derivatives transaction execution facility should provide to the public information regarding settlement prices, price range, trading volume, open interest and other related market information for all applicable contracts, as determined by the Commission. In making such determination, the Commission will consider whether a contract performs a significant price discovery function for transactions in the cash market for the commodity underlying the contract. The Commission will apply the same standards applicable to exempt boards of trade and exempt commercial markets (see §§36.2(b)(2) and 36.3(c)(2), respectively) whereby a market performs a significant price discovery function for transactions in the cash market for an underlying commodity if: (1) Cash market bids, offers or transactions are directly based on, or quoted at a differential to, the prices generated on the market on a more than occasional basis; or (2) the market's prices are routinely disseminated in a widely distributed industry publication and are routinely consulted by industry participants in pricing cash market transactions. In the event the Commission has reason to believe that a derivatives transaction execution facility may meet either of the foregoing standards, or if the facility holds itself out to the public as performing a price discovery function for the

cash market for the underlying commodity, the Commission shall notify the facility that it appears to meet the criteria for performing a significant price discovery function under Core Principle 5. Before making a final price discovery determination under this core principle, the Commission shall provide the facility with an opportunity for a hearing through the submission of written data, views and arguments. After consideration of all relevant matters, the Commission shall issue an order containing its determination whether the requirement of the core principle on publication of trading information under Section 5a(d)(5) of the Act applies to a particular contract traded on a facility. Provision of information for any applicable contract could be through such means as providing the information to a financial information service or by placing the information on a facility's Web site. Such information shall be made available to the public without charge no later than the business day following the day to which the information pertains.

Core Principle 6 of section 5a(d): *FITNESS STANDARDS*—*The board of trade shall establish and enforce appropriate fitness standards for directors, members of any disciplinary committee, members, and any other persons with direct access to the facility, including any parties affiliated with any of the persons described in this core principle.*

A derivatives transaction execution facility should have appropriate eligibility criteria for the categories of persons set forth in the core principle that would include standards for fitness and for the collection and verification of information supporting compliance with such standards. Minimum standards of fitness for persons who have member voting privileges, governing obligations or responsibilities, or who exercise disciplinary authority are those bases for refusal to register a person under section 8a(2) of the Act. In addition, persons who have governing obligations or responsibilities, or who exercise disciplinary authority, should not have a significant history of serious disciplinary offenses, such as those that would be disqualifying under §1.63 of this chapter. Eligible contract participants or eligible commercial entities who are members but do not have these privileges, obligations, responsibilities or disciplinary authority could satisfy minimum fitness standards by meeting the standards that they must meet to qualify under the Act's respective definitions of eligible contract participants or eligible commercial entities. Natural persons who directly or indirectly have greater than a ten percent ownership interest in a facility should meet the fitness standards applicable to members with voting rights. A demonstration of the fitness of the applicant's directors, members, or natural persons who directly or indirectly have greater than a ten

percent ownership interest in a facility may include providing the Commission with registration information for such persons, certification to the fitness of such persons, an affidavit of such persons' fitness by the facility's counsel or other information substantiating the fitness of such persons.

Core Principle 7 of section 5a(d) of the Act: *CONFLICTS OF INTEREST*—*The board of trade shall establish and enforce rules to minimize conflicts of interest in the decision making process of the derivatives transaction execution facility and establish a process for resolving such conflicts of interest.*

The means to address conflicts of interest in decision-making of a board of trade operating as a registered derivatives transaction execution facility should include methods to ascertain the presence of conflicts of interest and to make decisions in the event of such a conflict. The Commission also believes that a board of trade operating as a registered derivatives transaction execution facility should provide for appropriate limitations on the use or disclosure of material non-public information gained through the performance of official duties by board members, committee members and facility employees or gained through an ownership interest in the facility.

Core Principle 8 of section 5a(d) of the Act: *RECORDKEEPING*—*The board of trade shall maintain records of all activities related to the business of the derivatives transaction execution facility in a form and manner acceptable to the Commission for a period of 5 years.*

Section 1.31 of this chapter governs record-keeping obligations under the Act and the Commission's regulations thereunder. In order to provide broad flexible performance standards for recordkeeping, §1.31 was updated and amended by the Commission in 1999. Accordingly, §1.31 itself establishes the guidance regarding the form and manner for keeping records.

Core Principle 9 of section 5a(d) of the Act: *ANTITRUST CONSIDERATIONS*—*Unless necessary or appropriate to achieve the purposes of this Act, the board of trade shall endeavor to avoid—(A) adopting any rules or taking any actions that result in any unreasonable restraint of trade; or (B) imposing any material anti-competitive burden on trading on the derivatives transaction execution facility.*

A board of trade seeking to operate as a registered derivatives transaction execution facility may request that the Commission consider under the provisions of section 15(b) of the Act any of the board of trade's rules, which may be trading protocols or policies, and including both operational rules and the terms or conditions of products listed for trading, at the time it submits its registration application or thereafter. The Commission intends to apply section 15(b) of the Act to its consideration of issues under this core

principle in a manner consistent with that previously applied to contract markets.

[66 FR 42271, Aug. 10, 2001, as amended at 71 FR 1964, Jan. 12, 2006]

## PART 38—DESIGNATED CONTRACT MARKETS

Sec.

38.1 Scope.

38.2 Exemption.

38.3 Procedures for designation.

38.4 Procedures for listing products and implementing contract market rules.

38.5 Information relating to contract market compliance.

38.6 Enforceability.

APPENDIX A TO PART 38—GUIDANCE ON COMPLIANCE WITH DESIGNATION CRITERIA

APPENDIX B TO PART 38—GUIDANCE ON, AND ACCEPTABLE PRACTICES IN, COMPLIANCE WITH CORE PRINCIPLES

AUTHORITY: 7 U.S.C. 2, 5, 6, 6c, 7, 7a–2 and 12a, as amended by appendix E of Pub. L. 106–554, 114 Stat. 2763A–365.

SOURCE: 66 FR 42277, Aug. 10, 2001, unless otherwise noted.

### § 38.1 Scope.

The provisions of this part 38 shall apply to every board of trade that has been designated or is applying to become designated as a contract market under Sections 5 and 6 of the Act. *Provided, however*, nothing in this provision affects the eligibility of designated contract markets to operate under the provisions of parts 36 or 37 of this chapter.

[71 FR 1964, Jan. 12, 2006]

### § 38.2 Exemption.

Agreements, contracts, or transactions traded on a designated contract market under Section 5 of the Act, the contract market and the contract market's operator are exempt from all Commission regulations for such activity, except for the requirements of this part 38 and §§ 1.3, 1.12(e), 1.31, 1.37(c)–(d), 1.38, 1.52, 1.59(d), 1.60, 1.63(c), 1.67, 33.10, part 9, parts 15 through 21, part 40, part 41 and part 190 of this chapter, including any related definitions and cross-referenced sections.

[71 FR 1964, Jan. 12, 2006]

### § 38.3 Procedures for designation.

(a) *Application procedures.* (1) *Statutory (180-day) review procedures.* A board of trade desiring to be designated as a contract market shall file an application for designation with the Secretary of the Commission at its Washington, DC, headquarters. Except as provided under the 90-day review procedures described in paragraph (a)(2) of this section, the Commission will review the application for designation as a contract market pursuant to the 180-day timeframe and procedures specified in section 6(a) of the Act. The Commission shall approve or deny the application or, if deemed appropriate, designate the applicant as a contract market subject to conditions.

(i) The applicant must demonstrate compliance with the criteria for designation of section 5(b) of the Act, the core principles for operation of section 5(d) of the Act and the provisions of this part 38.

(ii) The application must include the following:

(A) A copy of the applicant's rules (as defined in § 40.1 of this chapter) and any technical manuals, other guides or instructions for users of, or participants in, the market, including minimum financial standards for members or market participants;

(B) A description of the trading system, algorithm, security and access limitation procedures with a timeline for an order from input through settlement, and a copy of any system test procedures, tests conducted, test results and contingency or disaster recovery plans;

(C) A copy of any documents describing the applicant's legal status and governance structure, including governance fitness information;

(D) An executed or executable copy of any agreements or contracts entered into or to be entered into by the applicant, including partnership or limited liability company, third-party regulatory service, or member or user agreements, that enable or empower the applicant to comply with a designation criterion or core principle (final, executed copies of such documents must be submitted prior to designation);